

The Director of Central Intelligence

Washington, D.C. 20505

12 September 1986

MEMORANDUM FOR: D/OGI/DDI

FROM: DCI

Dave,

The attached is interesting on the international financial structure.

William J. Casey

Attachment:

Clipping from The New York Times
29 August 1986

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THE NEW YORK TIMES, FRIDAY, AUGUST 29, 1986

Economic Scene

On Financial System Reform

E. Gerald Corrigan

HARDLY a day goes by when developments in the financial markets do not provide still another graphic illustration of the extent to which the speed, volume, value and complexity of financial transactions have increased. Indeed, while much has been written about this, the long-term implications for the structure and functioning of markets and institutions here and abroad are not easy to fully anticipate.

From what we have already witnessed, however, several things are clear:

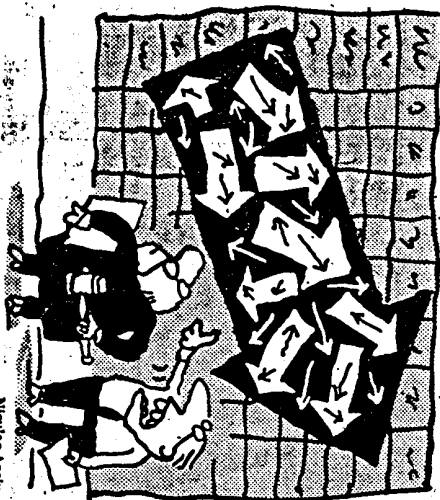
Technology and innovation have permitted the application of sophisticated forms of mathematics and computer technology in the financial marketplace. This has helped to foster new techniques, new instruments and trading and funding strategies that create complex operational, liquidity and credit interdependencies.

Money and capital markets are now truly international in character, operating in enormous size, around the clock and around the world.

In the United States, historic distinctions between certain classes of financial institutions have largely disappeared. While distinctions between "banks" and "thrift institutions" have been blurring for some time, it is now increasingly evident that the distinction between commercial banking and investment banking is also being eroded.

Perhaps even more fundamental, the distinction between "banking" and "commerce" is also being challenged. That is, whether it is via the acquisition of thrift units, nonbank banks or the expansion into "nonbank" financial activities, commercial concerns now have a major presence in the market place for the provision of financial, if not "banking," services.

While these and other trends provide clear op-



Nicholas Archib

portunities for greater efficiency and flexibility to both the suppliers and users of financial services, they also have worked to highlight differences in the supervisory, accounting, tax and regulatory treatment of transactions and institutions.

These trends have also accentuated the tendency to exploit loopholes in laws and regulations and, in the extreme, to undertake activities under the purview of the least supervisory resistance. While these tendencies are not new, the events of the past several years seem to convey not merely a difference in degree but, perhaps, in kind as well.

These developments beg for a coherent response by legislators and regulators alike. To some extent, this can be done within the framework of existing law, as for example, the continuing efforts to adapt bank supervisory standards and examination techniques to the changing environment.

However, it is doubtful that patchwork changes — whether supervisory or legislative — can constitute an effective response to the changes. What is needed is a broad-based and progressive overhaul of our Federal banking and related statutes and a greater degree of supervisory harmony internationally.

However, there are imposing barriers. For example, within the commercial banking industry —

to say nothing of the broader financial services industry — it has not been possible to carve out a general consensus on what constitutes an appropriate near-term or long-term approach.

The inability to reach such a consensus reflects, in part, the complexity of the issues, but it also stems from an apparent belief that certain interests would be better served by the current helter-skelter of events. Lacking a workable consensus, it is not surprising that the political process is also stalled.

On the international side, the barriers are even more formidable, in that they are often accentuated by even sharper differences in accounting, tax, legislative and regulatory considerations, as well as differences in tradition and culture.

While it is easy to understand why these barriers to change have been so difficult to overcome, those difficulties should not divert attention from the important public policy considerations associated with the operation of the banking and financial system. While some of these considerations, such as providing a measure of official protection to small investors and depositors, are relatively specific, others bearing on the stability of the system — and public confidence in it — are more vague, but ultimately more important.

Looked at in that light, the task is to blend together diverse public and private interests into a coherent view of the future structure of the financial system. As things now stand, there is a danger that events could elbow aside certain of those public interest considerations, thus undermining that necessary blend and doing so in ways that will not easily be remedied.

For that reason alone, but for others as well, the task of coming to grips with needed legislative reform at home and greater coordination abroad is so pressing.

E. Gerald Corrigan is president of the Federal Reserve Bank of New York.